



Beth A. Wood, CPA
State Auditor

STATE OF NORTH CAROLINA
Office of the State Auditor

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November 14, 2016

The Honorable Pat McCrory, Governor
The Honorable Representative George G. Cleveland
Mr. Keith Werner, State Chief Information Officer

This letter presents the results of our financial related audit of the Department of Information Technology (Department).

State Chief Information Officer Werner reviewed a draft copy of this report. His written comments start on page six.

The objective of this audit was to answer the questions, as listed in this report, asked by legislators and legislative staff about Department operations and activities. The audit scope was limited to the areas and time periods (state fiscal years 2014 and 2015) of legislative interest. For legislative reports, the audit scope was state fiscal year 2016.

To accomplish our audit objective, auditors performed procedures such as interviewing personnel, observing operations, reviewing policies, analyzing accounting records, and examining documentation supporting recorded transactions and operations.

As a basis for evaluating internal control, auditors applied the internal control guidance contained in professional auditing standards. However, our audit does not provide a basis for rendering an opinion on internal control, and consequently, we have not issued such an opinion.

We conducted this audit in accordance with generally accepted government auditing standards applicable to performance audits. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

We wish to express our appreciation to the staff of the Department of Information Technology for the courtesy, cooperation, and assistance provided us during the audit.

If you have any questions, please do not hesitate to contact my office.

A handwritten signature in cursive script that reads "Beth A. Wood".

Beth A. Wood, CPA
State Auditor

BACKGROUND

The North Carolina Department of Information Technology (Department) provides technology services to state agencies, public schools, community colleges, universities, and local governments. The Department receives State appropriations for infrastructure and administration, while services provided to users are funded through a fee-for-service, not-for-profit model. The goal of this model is full cost recovery with excess collections being returned to the users. To reach the goal of full cost recovery, the Department uses a rate-setting methodology that incorporates all costs, allocations, and estimated consumption of services.

The Department's broad service categories are:

- Hosting
- Network
- Telecommunications
- IT Architecture
- Desktop Computing
- Unified Communications (Including Email and Calendaring)
- Service Support
- IT Procurement
- Cybersecurity
- Application Development and Support

FINDINGS

1. DID THE DEPARTMENT OF INFORMATION TECHNOLOGY (DEPARTMENT) COMMINGLE THE IT FUND AND THE IT RESERVE FUND?

No. The Department did not technically commingle the IT Fund and the IT Reserve Fund.¹

Commingle would mean that the transactions of the two funds were accounted for in a single fund and that the transactions from each fund were indistinguishable from each other when spent.

While the IT Fund and the IT Reserve fund shared the same budget code,² they were assigned different cost center designations. An experienced budget and accounting professional could distinguish the transactions from each other by the use of the distinct cost center designations.³ For example: both the IT Fund and IT Reserve Fund shared budget code 24667 but the IT Fund had different cost center designations than the IT Reserve Fund. So an account number for the IT Fund would be 24667-2701 and the IT Reserve Fund would be 24667-2725, the 2701 and the 2725 being distinct cost center designations.⁴

However, inexperienced budget and accounting personnel and external users, such as the Departments non-accounting staff and legislators, could not and did not readily distinguish between the funds. This caused confusion, errors, and money spent in contradiction of the specific funding source or purpose.

2. DID THE DEPARTMENT ACCOUNT FOR AND SPEND MONEY IN ACCORDANCE WITH THE INTENT OF EACH FUND OR COST CENTER?

No. The Department spent money on items that were not permissible based on the intent (purpose) of the funding source.

During state fiscal years 2014 and 2015, there were multiple instances of expenses charged to the wrong cost center and/or fund. For example:

- The Department had a \$6 million contract for two separate IT projects with two distinct cost centers; however, only one cost center was charged
- A \$770,000 software licensing contract was incorrectly charged to the IT Fund when it should have been charged to the IT Reserve Fund
- A \$695,000 enterprise licensing agreement for use by multiple agencies was incorrectly charged to the IT Fund when it should have been charged to the IT Reserve Fund

¹ The IT Fund is for day-to-day operations of the Department. The IT Reserve Fund is for improvement and modernization of IT infrastructure.

² A budget code identifies major fund types and the responsible entity for reporting. The IT Fund and IT Reserve Fund are the only two funds within DIT that share a budget code.

³ Cost centers are department or activity centers within an agency. They are used to define funding sources, programs, expenses, grants, or other reporting needs.

⁴ IT Fund cost center numbers were 2701, 2705, 2715, 2720, 2735, 2740, 2750, 2760, 2780, 2790, and 2795. IT Reserve fund cost center numbers were 2725 and 2775.

FINDINGS

- A \$692,000 purchase of server equipment was charged to the wrong cost center within the IT Reserve Fund
- \$17,500 in salary for two employees was incorrectly charged to the IT Reserve Fund when it should have been charged to the IT Fund

3. DID THE DEPARTMENT FOLLOW STATE PROCUREMENT REGULATIONS FOR THREE SPECIFIC CONTRACTS?

Yes. The Department adhered to state procurement policies and procedures for the three specific procurement contracts.

Presidio - Telephone Equipment Contract

This contract complied with state procurement regulations.

The Department obtained an exemption from the State Chief Information Officer to waive competition and use an existing cooperative purchasing agreement.

Department files contained the appropriate approval and documentation of the justification⁵ for the waiver of competition exception, in accordance with state procurement regulations.

CDW Government – Computer Tablets

This contract complied with state procurement regulations.

The Department obtained approval from the State Chief Information Officer to not purchase computer tablets from the State's term contract vendors and purchase the tablets through an open solicitation process.

Department files contained the appropriate approval and documentation of the justification⁵ for the term contract exception as well as documents supporting the solicitation of competition (invitation for bids, actual bids, analysis of bids, award recommendation, and approved award), in accordance with state procurement regulations.

Multiple Vendors – IT Staffing

This contract complied with state procurement regulations.

The Department wanted to approve multiple vendors (about 200) to put on a pre-approved vendor list of IT professionals so that agencies could quickly contract for temporary IT staffing. To approve a vendor, the Department had to define the job skills required and analyze bids to ensure the job skills were met.

Department files contained the appropriate documentation to support the solicitation for bids, analysis of bids, award recommendations, and approval of vendors, in accordance with state procurement regulations.

⁵ The audit of the contract was limited in scope to whether the waiver was allowable in accordance with state procurement policies. No opinion is rendered on the rationale of the actual justification and potential cost savings of the waiver.

FINDINGS

4. DID THE DEPARTMENT ESTABLISH CONSISTENT, FULLY TRANSPARENT, EASILY UNDERSTANDABLE RATES FOR EACH SERVICE?

No. The Department leadership did not establish consistent, fully transparent, easily understandable rates for each service.

The Department cannot explain how it established rates for 94 of the 158 (59%) service rates for state fiscal year 2016. This lack of clarity remains even though the Department paid two vendors approximately \$1.3 million in total to develop rate setting methodology and recommend service rates.

Seventy-nine of the 94 unsupported rates were unexplained deviations from a vendor-provided rate methodology and recommendation. The remaining 15 unsupported rates were independently developed by the Department but were not supported with calculations, details, or documentation.

5. WERE DEPARTMENT REPORTS PROVIDED TO OUTSIDE USERS TIMELY AND USEFUL?

Reports provided to outside users were generally timely, but were not considered particularly useful by recipients.

The General Assembly's Joint Legislative Oversight Committee on Information Technology (Committee) and Fiscal Research Division (Fiscal Research) are the primary recipients of Department reports.

For State fiscal year 2016, the Department submitted 27 of 29 (93%) of the required reports on time. For the two reports provided late, the Department provided users advance notice and reason for the delay. The two late reports were provided within 60 days of the due date.

Report recipients suggested and agreed that the reporting requirements were voluminous and not particularly useful. Due to limited responses, an opinion on which particular reports are useful could not be determined. However, the limited responses indicated that the volume and content of reports should be revisited to ensure that future reports are useful.

6. WAS A FORMER DEPARTMENT EMPLOYEE HIRED AND EVALUATED IN ACCORDANCE WITH STATE POLICY?

Documentation supports that the former Department employee was hired and evaluated in accordance with state policy.

The former employee's file contained documentation of a competency analysis, summary of job duties, salary recommendation, salary equity analysis, and approval for the hiring offer.

FINDINGS

Also, the former employee received annual performance evaluations that corresponded with their tenure. Documentation shows that the performance evaluations were completed in accordance with state policy.

Auditors did not perform procedures to determine the quality of the Department's hiring decision or performance evaluation process.

RESPONSE FROM DEPARTMENT OF INFORMATION TECHNOLOGY



PAT MCCRORY
Governor
KEITH WERNER
Secretary of Information Technology
State Chief Information Officer

November 7, 2016

The Honorable Beth A. Wood
Office of the State Auditor
20601 Mail Service Center
Raleigh, North Carolina 27699-0601

Dear Ms. Wood:

We have reviewed your results of our financial related audit of the Department of Information Technology. The audit scope was limited to the areas and time periods (state fiscal years 2014 and 2015) of legislative interest. For legislative reports, the audit scope was state fiscal year 2016. We respond to the State's recommendations as follows:

Finding # 1. DID THE DEPARTMENT OF INFORMATION TECHNOLOGY (DEPARTMENT) COMMINGLE THE IT FUND AND THE IT RESERVE FUND?

OSA's Response: No. The Department did not technically commingle the IT Fund and the IT reserve Fund.

DIT's Response: DIT agrees with the finding.

Finding #2: DID THE DEPARTMENT ACCOUNT FOR AND SPEND MONEY IN ACCORDANCE WITH THE INTENT OF EACH FUND OR COST CENTER?

OSA's Responses: No. The Department spent money on items that were not permissible based on the intent (purpose) of the funding source.

DIT's Response: DIT agrees with the finding.

DIT currently has a review process that requires the coding of expenditures to the appropriate Fund and Cost Center for which they were intended. The DIT financial division plans to implement a budgeting 101 education training, led by the budget manager, to be held no later than the summer of 2017 that will focus on how funding should be expensed. DIT will also continue to collaborate with OSBM in order to properly identify the appropriate cost centers and /or funds to expense.

Finding #3: DID THE DEPARTMENT FOLLOW STATE PROCUREMENT REGULATIONS FOR THREE SPECIFIC CONTRACTS?

OSA's Response: Yes. The Department adhered to state procurement policies and procedures for the three specific procurement contracts.

DIT's Response: DIT agrees with the finding.

The logo for 'Nothing Compares' features a stylized blue wave or mountain shape above the text 'Nothing Compares' in a blue, sans-serif font.
State of North Carolina | Information Technology
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Raleigh, North Carolina 27699

RESPONSE FROM DEPARTMENT OF INFORMATION TECHNOLOGY



PAT MCCRORY
Governor

KEITH WERNER
Secretary of Information Technology
State Chief Information Officer

Finding #4: DID THE DEPARTMENT ESTABLISH CONSISTENT, FULLY TRANSPARENT, EASILY UNDERSTANDABLE RATES FOR EACH SERVICE?

OSA's Response: The Department leadership did not establish consistent, fully transparent, easily understandable rates for each service.

DIT's Response: DIT agrees with the finding.

The DIT financial division is currently reviewing and determining the most appropriate rates calculation methodology in order to ensure clarity and transparency of all rates to customers. The first iteration of the new rates methodology will be implemented, upon OSBM approval, by the DIT rates team during the FY 2018-2019 budget process. The entire implementation of the approved new methodology is anticipated during the following biennium.

Finding #5: WERE DEPARTMENT REPORTS PROVIDED TO OUTSIDE USERS TIMELY AND USEFUL?

OSA's Response: Reports provided to outside users were generally timely, but were not considered particularly useful by recipients.

DIT's Response: DIT agrees with the finding.

Finding #6. WAS A FORMER DEPARTMENT EMPLOYEE HIRED AND EVALUATED IN ACCORDANCE WITH STATE POLICY?

OSA's Response: Documentation supports that the former Department employee was hired and evaluated in accordance with state policy.

DIT's Response: DIT agrees with the finding.

Sincerely,

A handwritten signature in black ink, appearing to read 'Keith Werner'.

Keith Werner

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For additional information contact:
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919-807-7513



This audit required 2559 hours at an approximate cost of \$257,939.